MULTIMEDIA UNIVERSITY

STUDENT ID NO

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FINAL EXAMINATION

TRIMESTER 2, 2015/2016

BAC2664 – AUDITING

(All sections / Groups)

2 MARCH 2016
2.30p.m – 5.30p.m
(3 Hours)

INSTRUCTIONS TO STUDENTS

1. This Question paper consists of 4 pages (excluding cover page) with 5 Questions only.

2. Attempt **ALL FIVE** questions.

3. Marks allocations are shown at the end of each question.

Question 1

(a) Abas & Co is an audit firm which has seen its revenue decline steadily over the past few years. The firm is looking to increase its revenue and client base therefore has developed a new advertising strategy where it has guaranteed that its audits will minimise disruption to companies as they will not last longer than two weeks. In addition, Abas & Co has offered all new audit clients a free accounts preparation service for the first year of the engagement, as it is believed that time spent on the audit will be reduced if the firm has produced the financial statements.

The audit firm is seeking to reduce audit costs and has therefore decided not to update the engagement letters of existing clients, on the basis that these letters do not tend to change much on a yearly basis. One of Abas & Co's existing clients has proposed that this year's audit fee should be based on a percentage of their final pre-tax profit. The partners are excited about this option as they believe it will increase the overall audit fee. Abas & Co has recently obtained a new audit client, Maju Bhd, whose year end is 31 December 2014. Maju Bhd requires their audit to be completed by the end of February 2015; however, this is a very busy time for Abas & Co and so it is intended to use more junior staff as the senior auditors are not available. Additionally, in order to save time and cost, Abas & Co has not contacted Maju Bhd's previous auditors.

Required:

Describe the steps that Abas & Co should take in (i) and (ii) below, in relation to Maju Bhd:

(i) Prior to accepting the audit; (5 marks)

(ii) To confirm whether the preconditions for the audit are in place. (5 marks)

(iii)State SIX matters that should be included in the usual audit engagement letter. (3 marks)

(b)

(i) Define a 'test of control' and provide an example of a test of control in relation to the audit of wages and salaries. (2 marks)

(ii) Define a 'substantive procedure' and provide an example of a substantive procedure in relation to the audit of wages and salaries. (2 marks)

Continued....

(iii) ISA 500 Audit Evidence requires auditors to obtain sufficient and appropriate audit evidence. Appropriateness is a measure of the quality of audit evidence; that is, its relevance and its reliability.

Required:
Explain THREE factors which influence the reliability of audit evidence. (3 marks)

(Total : 20 marks)

Question 2

Comel Bhd (Comel) manufactures tinned fruit and vegetables which are supplied to large and small food retailers. Management and those charged with governance of Comel have concerns about the effectiveness of their sales and despatch system and have approached your audit firm to document and review the system.

Sales and despatch system

Sales orders are mainly placed through Comel's website but some are made via telephone. Online orders are automatically checked against inventory records for availability; telephone orders, however, are checked manually by order clerks after the call.

A follow-up call is usually made to customers if there is insufficient inventory. When taking telephone orders, clerks note down the details on plain paper and afterwards they complete a three part pre-printed order form. These order forms are not sequentially numbered and are sent manually to both despatch and the accounts department.

As the company is expanding, customers are able to place online orders which will exceed their agreed credit limit by 10%. Online orders are automatically forwarded to the despatch and accounts department. A daily pick list is printed by the despatch department and this is used by the warehouse team to despatch goods.

The goods are accompanied by a despatch note and all customers are required to sign a copy of this. On return, the signed despatch notes are given to the warehouse team to file. The sales quantities are entered from the despatch notes and the authorised sales prices are generated by the invoicing system. If a discount has been given, this has to be manually entered by the sales clerk onto the invoice. Due to the expansion of the company, and as there is a large number of sale invoices, extra accounts staff have been asked to help out temporarily with producing the sales invoices. Normally it is only two sales clerks who produce the sales invoices.

Required:
(a) Describe TWO methods for documenting the sales and despatch system; and for each explain an advantage and a disadvantage of using this method. (6 marks)

(b) List TWO control objectives of Comel Bhd's sales and despatch system. (2 marks)

Continued....

(c) Identify and explain SIX deficiencies in Comel Bhd's sales and despatch system and provide a recommendation to address each of these deficiencies. (12 marks)

(Total 20 marks)

Question 3

(a)Explain the concept of TRUE and FAIR presentation. (4 marks)

(b) According to Companies Act 1965, Sec 174(1), every auditor of a company shall report to the members on the accounts required to be laid before the company at the General Meeting and on the company's accounting and other records relating to those accounts.

Required:
Explain the duties, powers and rights of an external auditor as stated in the Companies Act 1965. (16 marks)

(Total 20 marks)

Question 4

Waja Bhd specialises in manufacturing equipment which can help to reduce toxic emissions in the production of chemicals. The company has grown rapidly over the past eight years and this is due partly to the warranties that the company gives to its customers. It guarantees its products for five years and if problems arise in this period it undertakes to fix them, or provide a replacement product. You are the manager responsible for the audit of Waja Bhd and you are performing the final review stage of the audit and have come across the following two issues.

Receivable balance owing from Permata Bhd
Waja Bhd has a material receivable balance owing from its customer, Permata Bhd. During the year-end audit, your team reviewed the ageing of this balance and found that no payments had been received from Permata Bhd for over six months and Waja Bhd would not allow this balance to be circularised. Instead management has assured your team that they will provide a written representation confirming that the balance is recoverable.

Warranty provision
The warranty provision included within the statement of financial position is material. The audit team has performed testing over the calculations and assumptions which are consistent with prior years. The team has requested a written representation from management confirming the basis and amount of the provision are reasonable. Management has yet to confirm acceptance of this representation.

Required:
(a) Briefly explain FIVE audit procedures required in respect of accounting estimates. (5 marks)

Continued....

(b) For each of the two issues above:

(i) Discuss the appropriateness of written representations as a form of audit evidence. (4 marks)

(ii) Describe additional procedures the auditor should now perform in order to reach a conclusion on the balance to be included in the financial statements. (6 marks)

(c) The directors of Waja Bhd have decided not to provide the audit firm with the written representation for the warranty provision as they feel that it is unnecessary.

Required:

Explain the steps the auditor of Waja Bhd should now take and the impact on the audit report in relation to the refusal to provide the written representation. (5 marks)

(Total 20 marks)

Question 5

(a) Explain the four categories of audit reports below:

(i) Standard unqualified (also include explanation on the conditions need to be met). (6 marks)

(ii) Unqualified with explanatory paragraph or modified wording. Provide THREE examples when an explanatory paragraph or modified wording should be used in an unqualified opinion. (4 marks)

(iii) Qualified (2 marks)

(iv) Adverse or Disclaimer (2 marks)

(b) Describe TWO substantive procedures the auditor should adopt to verify EACH of the following assertions below in relation to an entity's property, plant and equipment.

(i) Valuation

(ii) Completeness

(iii) Rights and obligations

(6 marks)

(Total 20 marks)

-End of Questions-